

**PROVIDER REIMBURSEMENT REVIEW BOARD
DECISION
ON THE RECORD
2003-D12**

PROVIDER – Susquehanna Regional
Home Health Services
Williamsport, Pennsylvania

Provider No. 39-7006

vs.

INTERMEDIARY – Blue Cross and
Blue Shield Association/Cahaba
Government Benefits Administrator



DATE OF HEARING -
November 27, 2002

Cost Reporting Periods Ended
June 30, 1995

CASE NO. 97-1686

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ISSUE:

Was the Intermediary's adjustment to rent paid by the Provider to a related party proper?

STATEMENT OF THE CASE AND PROCEDURAL HISTORY:Governing Statutes and Regulations:

This dispute arises out of the Intermediary's determination to disallow part of the Provider's lease payments made to a related party.

The Medicare program was established in 1965 under Title XVIII of the Social Security Act (the Act) to provide health insurance to the aged and disabled. 42 U.S.C. §§ 1395 – 1395cc. The Health Care Financing Administration ("HCFA") (now Centers for Medicare and Medicaid Services) ("CMS") is the operating component of the Department of Health and Human Services charged with administering the Medicare program.

In order to participate in the Medicare program, a hospital must file a provider agreement with the Secretary. 42 U.S.C. § 1395cc. The Secretary's payment and audit functions under the Medicare program are contracted out to insurance companies known as fiscal intermediaries. Fiscal intermediaries determine payment amounts due the providers under the Medicare law and under interpretative guidelines published by CMS. *Id.*

At the close of its fiscal year, a provider must submit a cost report to the fiscal intermediary showing the costs it incurred during the fiscal year and what portion of those costs are to be allocated to Medicare. 42 C.F.R. § 413.20. The fiscal intermediary audits the cost reports and determines the total amount of Medicare reimbursement due the provider, which it publishes in a notice of program reimbursement ("NPR") that sets forth the individual expenses allowed and disallowed by the intermediary. 42 C.F.R. § 405.1803. A provider dissatisfied with the intermediary's final determination of total reimbursement may file an appeal with the Provider Reimbursement Review Board ("Board") within 180 days of the NPR. 42 U.S.C. § 1395oo(a); 42 C.F.R. § 405.1835.

Under Medicare regulations, a provider is entitled to claim costs applicable to services, facilities, and supplies furnished to the provider by organizations related to the provider by common ownership or control at the cost to the related organization as long as the cost does not exceed the price of services or supplies that could be purchased elsewhere. 42 C.F.R. § 413.17. However, there is an exception to this rule. 42 C.F.R. § 413.17(d)(1), provides that the charge made by the related supplier to the Provider is allowable as "cost" provided the following criteria are met:

- (i) The supplying organization is a bona fide separate organization;

- (ii) A substantial part of its business activity is transacted with others than the provider and organizations related to the supplier and there is an open competitive market for the type of services furnished by the organization;
- (iii) The services are those that commonly are obtained by institutions such as the provider from other organizations and are not a basic element of direct patient care;
- (iv) The charge to the provider is in line with the charge of services in the open market by the supplier to the provider.

The HCFA Manual at HCFA Pub. 15-1 § 1010 sets out the same criteria. The question before the Board is whether or not the Provider qualifies for the exception to the related organization principle in accordance with Medicare regulations and instructions.

Background:

Susquehanna Regional Home Health Services (“SRHHS”) (“Provider”) is a freestanding home health agency located in Williamsport, Pennsylvania that was certified for Medicare on July 1, 1970. The Intermediary (Cahaba Government Benefits Administrators) issued the NPR on September 27, 1996, and the Provider filed its appeal timely with the Board on March 23, 1997, pursuant to 42 C.F.R. § § 405.1835 - .1841. The Medicare reimbursement effect is approximately \$21,502.¹

In its as-filed cost report, the Provider claimed \$95,530 in lease expense paid to a related organization, Grampian Boulevard Corporation (“GBC”). The Intermediary determined that the lease expense of \$95,530 was not the actual cost to the related lessor and reduced this amount to \$62,521. In reviewing GBC’s financial statements, the Intermediary determined the total expense incurred for the operation of the building was \$388,169 for the year in question.² The Intermediary then calculated the cost per square foot by dividing the total building expenses incurred by total square footage of the building (40,610.78) and found it to be \$9.55583; the cost per square foot was then multiplied by 6,541, the square footage occupied by the Provider.³ This methodology permitted \$62,521 of allowable lease cost and subjected the Provider to a disallowance of \$33,009.⁴

The Provider was represented by John F. Bubb, Manager of Corporate Finance, of Susquehanna Health System. The Intermediary was represented by Bernard M. Talbert, Esquire, of the Blue Cross and Blue Shield Association.

¹ See Intermediary’s position paper at 5.

² See Intermediary’s position paper Exhibit I-2.

³ See Intermediary’s position paper Exhibit I-2.

⁴ See Provider’s position paper Exhibit P-9.

PROVIDER'S CONTENTIONS:

The Provider does not dispute the Intermediary's calculations but it contends that the amount of related party lease expense claimed on its Medicare cost report met the requirements for an exception established in HCFA Pub. 15-1 § 1010, based on the following:

1. "The supplying organization must be a unique, separate organization."

GBC is, in fact, a separate company with a board of directors completely independent from the SRHHS board of directors. There are no individuals that sit on both boards.

2. "A substantial part of the supplying organization's business activity is transacted with other organizations not related to the provider, and there is an open and competitive market."

GBC is a real estate holding company that leases space to independent physician practices as well as Divine Providence Hospital ("DPH") and a doctor practice, Grampian Health Services ("GHS"), both of whom are related parties to GBC and SRHHS through common ownership.

3. "The services, facilities, or supplies are those which commonly are obtained by institutions such as the provider from other organizations and are not a basic element of patient care ordinarily furnished directly to patients by such institutions."

Due to the growth of visits and increasing staff, SRHHS needed additional space, prompting the relocation to a new building with 6,564 square feet.⁵ This need for additional space was met by leasing space in lieu of purchasing a building in which to operate. Typically, space needs are often met by leasing from other parties.

4. "The charge to the provider is in line with the charge for such facilities in the open market."

⁵ The old building consisted of 3,480 square feet.

The rental rate to SRHHS includes all utilities, housekeeping, maintenance services, and free-accessible parking. The Provider contends that the lease rate is competitive in the open market. For example, Divine Providence MRI, a for-profit joint venture of GHS,⁶ incurred the same rate. The Provider asserts that unrelated parties would have been charged comparable rates.

Therefore, the Provider believes that it qualified for an exception based on the criteria set forth in the regulations and HCFA Pub. 15-1 § 1010.

INTERMEDIARY'S CONTENTIONS:

The Intermediary contends that its adjustment was made in accordance with HCFA Pub. 15-1 § 1000, Costs to Related Organizations, which states:

[c]osts applicable to services, facilities, and supplies furnished to the provider by organizations related to the provider by common ownership or control are includable in the allowable cost of the provider at the cost to the related organization.

The Intermediary noted that the lease expense claimed by the Provider to GBC had not been reduced to actual cost; therefore, an adjustment was necessary in accordance with HCFA Pub. 15-1 § 1000.

Initially, the Intermediary asserted that it was not provided sufficient documentation to make a thorough evaluation of each of the criteria set forth in the regulation and HCFA Pub. 15-1 § 1010.

After review of the Provider's correspondence dated November 27, 1995,⁷ the Intermediary contends that the Provider does not qualify for the related party exception since only 44% of GBC's revenue was generated from unrelated entities. The Intermediary insists that, in accordance with HCFA Pub. 15-1, § 1010(b), a substantial part of the supplying organization's business activity must be transacted with other organizations not related to the provider. In this case, 56% of GBC's revenue was from leases by related entities. Therefore, under these circumstances, the Provider does not meet the necessary criterion set forth under the Medicare instructions and guidelines.

CITATION OF LAW, REGULATIONS AND PROGRAM INSTRUCTIONS:

1. Law - 42 U.S.C.:

§ 1395 et seq. - Prohibition against any

⁶ GHS is one of the three general partners of Divine Providence MRI.

⁷ See Intermediary's position paper Exhibit I-1.

Federal Interference

2. Regulations - 42 C.F.R.:

- §§ 405.1835 -.1841 - Board Jurisdiction
- § 413.20 - Financial Data and Reports
- § 405.1803 - Intermediary Determination and NPR
- § 413.17 et seq. - Cost to Related Organization

3. Program Instructions-Provider Reimbursement Manual, Part I (HCFA Pub. 15-1):

- § 1000 - Cost to Related Organizations
- § 1010 et seq. - Exception to the Related Organization Principle

FINDINGS OF FACT, CONCLUSIONS OF LAW AND DISCUSSION:

After consideration and analysis of the Medicare regulations and manual guidelines, the parties' contentions and evidence presented, the Board finds and concludes that the Provider does not qualify for an exception to the related organization principle in accordance with 42 C.F.R. § 413.17. There is no dispute that the Provider and GBC are related, but separate entities. The dispute arises as to whether or not the Provider meets the regulatory criteria for an exception to the related party principle.

42 C.F.R. § 413.17 states in part, that if a Medicare provider purchases services from a related organization, those costs will only be reimbursed to the provider at the cost of the related organization. Section 413.17 also contains an exception provision, which allows a provider to be reimbursed to the extent of supplier charges, provided four specific criteria are met.

The Board finds that the Provider is not entitled to an exception to the related organization principle as it did not meet the criterion of 42 C.F.R. § 413.17(d)(1)(ii), which provides:

[a] substantial part of business activity is transacted with other than the Provider and organizations related to the supplier. . .

In this case, the record indicates that approximately 44% of GBC's revenue was transacted with unrelated parties.⁸ Neither the regulations nor the Medicare program instructions specify a particular standard of measurement for defining the term "substantial part" as used in the regulation above. However, Medicare program instructions in HCFA Pub. 15-1 § 1000 clarify the Cost To Related Organizations regulation (42 C.F.R. § 413.17) by stating in part:

[t]he purpose of this principle is two-fold:
(1) to avoid the payment of a profit factor to the provider through the related organization (whether) related by common ownership or control), and (2) to avoid payment of artificially inflated costs, which may be generated from less than arm's length bargaining.

Also, HCFA Pub. 15-1, § 1010.1 entitled *Examples of Applying the Exception* states:

[t]he exception is intended to cover certain situations where large quantities of goods and services are supplied to the general public and only *incidentally* are furnished to related organizations. (emphasis added).

Based on the above, the Board finds that the Provider's argument that 44% represents a "substantial" part of its business activity is without merit and the Provider is not entitled to an exception to the Cost To Related Organizations regulation in 42 C.F.R. § 413.17.

DECISION AND ORDER:

The Intermediary's determination that the Provider did not meet the criteria for an exception to the Cost To Related Organizations regulation is correct. The Intermediary's adjustment to reduce the lease expense is affirmed.

BOARD MEMBERS PARTICIPATING:

Suzanne Cochran, Esquire
Henry C. Wessman, Esquire
Stanley J. Sokolove
Gary Blodgett, D.D.S.

⁸ See Provider's position paper Exhibit P-1.

DATE OF DECISION: January 8, 2003

FOR THE BOARD:

Suzanne Cochran, Esquire
Chairperson